IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

No. 11173

SECURITIES AND EXCHANGE COMMISSION,
Appellant,

v.

THE PENFIELD COMPANY OF CALIFORNIA and
A. W. YOUNG,
Appellees.

BRIEF FOR APPELLANT

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PAUL P. O'BRIEN,
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ROGER S. FOSTER,
Solicitor,
ROBERT S. RUBIN,
Assistant Solicitor,
W. VICTOR RODIN,
Attorney,
Securities and Exchange Commission,
18th and Locust Streets,
Philadelphia 3, Pa.

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STATEMENT OF JURISDICTION

This is an appeal from a final order entered in a civil contempt proceeding in the District Court for the Southern District of California, Central Division, on July 2, 1945 (R. 19).[1] This order fined appellee, A. W. Young, secretary-treasurer of appellee, The Penfield Company of Cali-

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[1] Section 22(b) of the Securities Act of 1933 (15 U.S.C. 77v(b)) provides:

"In case of contumacy or refusal to obey a subpena issued to any person, any of the said United States courts, within the jurisdiction of which said person guilty of contumacy or refusal to obey is found or resides, upon application by the Commission may issue to such person an order requiring such person to appear before the Commission, or one of its examiners designated by it, there to produce documentary evidence if so ordered, or there to give evidence touching the matter in question; and any failure to obey such order of the court may be punished by said court as a contempt thereof."

fornia ("Penfield"), a corporation, $50 for contempt, the court rejecting the Commission's request for a coercive decree. Young was adjudged in contempt for disobeying an order of the district court which had been affirmed by this Court, directing him to produce certain books and records of Penfield pursuant to a subpœna *duces tecum* issued by the Commission.

The jurisdiction of this Court is invoked under Section 128 of the Judicial Code, as amended (28 U.S.C. 225), made applicable by Section 22(a) of the Securities Act of 1933 (15 U.S.C. 77v(a)) (the "Act").

STATEMENT OF FACTS

The Commission, pursuant to Section 20(a) of the Act (15 U.S.C. 77t(a)), issued an order on May 14, 1942, and supplemental orders on February 13, 1943, and April 8, 1943, directing an investigation to determine whether a number of specified companies and persons (Penfield and Young being added in the April 1943 supplemental order) had violated Sections 17(a) and 5(a) of the Act (15 U.S.C. 77q(a) and 77e(a)) in the sale of stock of Penfield and other securities by means of untrue statements of material facts and without registration (R. 2-3, 7; see *Penfield Co. of California* v. *S.E.C.*, 143 F. 2d 746, 747-8 (C.C.A. 9, 1944), cert. denied 323 U.S. 768). In the course of this investigation and pursuant to Section 19(b) of the Act (15 U.S.C. 77s(b)) the Commission directed a subpœna *duces tecum* to Young, as an officer of Penfield (R. 3-4). The subpœna required the production of certain books and records of Penfield covering the four-year period from May 1, 1939, to the date of the subpœna (April 9, 1943). *Penfield Co. of California* v. *S.E.C.*, *supra*, at 748. Upon Young's refusal to appear and produce the specified books and records, the Commission on April 13, 1943, filed an application in the district court for an order enforcing the subpœna (R. 2, 4; see R. 79).

On June 1, 1943, after hearing, the court granted the Commission's application, specifically ordering Young as secretary-treasurer of Penfield to produce the specified items on June 8, 1943, and at any adjournment dates; and further ordered, pursuant to a stipulation by the parties, that the books and records, in lieu of their physical production at the office of the Commission, should be made available in the office of Penfield to such officer and employees of the Commission as might be designated for such purpose (R. 4-5, 11-15; see R. 3, 7-8). Penfield appealed from this order and, on June 30, 1944, this Court affirmed. 143 F. 2d 746. A petition for a writ of certiorari was denied by the Supreme Court on November 6, 1944. 323 U.S. 768. On November 13, 1944, the mandate of this Court was issued affirming said order of June 1, 1943, and on December 7, 1944, said mandate was filed and spread upon the minutes of the district court (R. 5).

Despite affirmance of this order on appeal the net result of the proceedings to date is that the Commission has been unable to secure compliance. Appellees are permitted to continue to frustrate a federal court order even after its legality has been fully confirmed on appeal. This Court's mandate spread on the district court's records after the Supreme Court had denied certiorari most assuredly put at rest any doubt as to appellees' legal obligation to comply. Following the mandate a designated officer of the Commission on January 16, 1945, addressed and mailed a communication to Young and his attorneys advising that this officer would call at the office of Penfield in Los Angeles on January 24, 1945, for the purpose of examining the books and records referred to in the district court's order of June 1, 1943 (R. 6, 9-10; see R. 80). On January 24, 1945, the said officer and another designated officer of the Commission presented themselves at the office of Penfield and demanded to see the specified books and records but such demand was refused (R. 6-7).

On January 24, 1945, the Commission instituted civil contempt proceedings against Young in the district court

by filing a proposed rule to show cause why Young should not be adjudged in contempt, together with an affidavit in support of the rule (R. 2-15). The court below declined to issue the rule immediately but instead directed Young to show cause on February 5, 1945, why a further order should not be made directing Young to show cause why an order should not be made holding him in contempt of court (R. 15-16; 31). After hearing both sides on February 8, 1945, the court expressed doubt as to whether the Commission was entitled to obtain the evidence sought for until after the conclusion of a pending criminal trial involving Young, Penfield and others [2] because that evidence might be used by the Government (R. 72, 73). The court issued an order to show cause returnable on February 26, 1945 (R. 17-18), and stated that it would on that date decide whether or not to proceed with the contempt proceedings or postpone the matter until after the criminal trial (R. 76).

On February 26, 1945, the court, over objection of Commission counsel, postponed the hearing on the order to show cause to May 28, 1945, then to June 25, 1945, and then to July 2, 1945, when the matter finally came on to be heard (R. 80-1), and on that date the court below adjudged Young to be in contempt, but refused to grant a remedial decree calculated to coerce production of Penfield's books and records (R. 86). Instead, the court ordered Young merely to "pay a fine of $50, and stand committed until paid", with execution stayed temporarily, presumably to give Young an opportunity to pay the $50 (R. 87). It is from this order that the Commission appeals.

SPECIFICATION OF ERROR

The court below erred in refusing to enter a remedial order calculated to coerce production of the records. The contempt proceeding was instituted by the Commission to obtain compliance with an order of the district court re-

[2] See note 4, *infra*.

quiring Young to produce certain books and records of Penfield pursuant to a subpœna issued by the Commission under the Securities Act of 1933. The proceeding was civil in nature, and upon a finding of contempt, the court should have entered a remedial and coercive decree designed to obtain compliance, instead of the mere penalty for past dereliction which the court imposed.

ARGUMENT

The Contempt Proceeding Was Civil in Nature and Therefore, Having Found Young in Contempt, the Court Below Erred in Failing to Enter a Remedial and Coercive Decree.

The instant proceeding, which was instituted by the Commission against Young to obtain compliance with the district court's order of June 1, 1943, directing production of the records, was one for civil contempt. It is captioned as a civil action (R. 2, 11, 25). It was called on the civil calendar (R. 77). Counsel for the Commission stated that the proceeding was for civil contempt (R. 35-39, 43, 77).[3] It meets the tests laid down by the courts in determining that a contempt proceeding is civil in nature. It was instituted by the Commission, not by the United States nor by the court to vindicate its authoriy. *McCrone* v. *United States*, 307 U.S. 61 (1939); *Western Fruit Growers, Inc.*, v. *Gotfried*, 136 F. 2d 98, 100-01 (C.C.A. 9, 1943); *McCann* v. *New York Stock Exchange*, 80 F. 2d 211, 214 (C.C.A. 2, 1935), cert. denied 299 U.S. 603; *Norstrom* v. *Wahl*, 41 F. 2d 910, 913 (C.C.A. 7, 1930). It was a continuation of the earlier civil action in the district court to enforce the Commission's subpœna (see R. 77-8), and was a step in the enforcement of the district court's order of June 1, 1943 (which this Court had affirmed). *N.L.R.B.* v. *Hopwood Retinning Co.*, 104 F. 2d 302, 305 (C.C.A. 2, 1939); *Gompers* v. *Bucks Stove & Range Co.*, 221 U.S. 418, 444-5 (1911); cf. *I.C.C.* v. *Brimson*, 154 U.S. 447, 470 (1894). Its purpose was remedial, to obtain compliance with the subpœna enforcement order. *N.L.R.B.* v. *Hopwood Retinning Co.*, *supra*, at 305; *N.L.R.B.* v. *Carlisle Lumber Co.*, 108 F. 2d 188 (C.C.A. 9, 1939); *McCrone* v. *United States*, *supra*, at

[3] Counsel for Young recognized the civil nature of the proceeding by citing the Rules of Civil Procedure to support one of his contentions at the February 8, 1945, hearing (R. 27).

64. Upon a judgment for civil contempt, the punishment must be remedial and for the benefit of the complainant. *McCann* v. *New York Stock Exchange, supra; Norstrom* v. *Wahl, supra.*

Having adjudged Young to be in contempt in a civil contempt proceeding, the court below had no discretion but to impose a remedial, coercive penalty designed to compel compliance with the mandate of this Court. *Oriel* v. *Russell,* 278 U.S. 358 (1929) ; *Gompers* v. *Bucks Stove & Range Co.,* 221 U.S. 418 (1911) ; *Clarke* v. *Federal Trade Commission,* 128 F. 2d 542 (C.C.A. 9, 1942). In the *Clarke* case, the Federal Trade Commission subpœnaed a witness to appear and testify at a hearing before that commission. The witness appeared but declined to answer any questions. The Federal Trade Commission obtained a subpœna enforcement order in the district court. The witness disobeyed the order by refusing to answer a certain question put to him. The commission instituted civil contempt proceedings, and the witness was adjudged in contempt and committed until he should answer the particular question. On appeal, this Court affirmed the contempt order, saying at page 543:

> "The party or the witness has no alternative but to obey or be held in contempt".

Since, in the instant case, the order of June 1, 1943, affirmed by this Court, required performance of an affirmative act, namely, the production of Penfield's books and records, the proper penalty was imprisonment unless and until the order was complied with. *Gompers* v. *Bucks Stove & Range Co., supra; Clarke* v. *Federal Trade Commission, supra.* In the *Gompers* case the court said, at page 442:

> ". . . Imprisonment for civil contempt is ordered where the defendant has refused to do an affirmative act required by the provisions of an order which, either in form or substance, was mandatory in its character. Imprisonment in such cases is not inflicted as a punishment, but is intended to be remedial by coercing the

> defendant to do what he had refused to do. The decree in such cases is that the defendant stand committed unless and until he performs the affirmative act required by the court's order. * * * If imprisoned, as aptly said in *In re Nevitt*, 117 Fed. Rep. 451, 'he carries the keys of his prison in his own pocket.' He can end the sentence and discharge himself at any moment by doing what he had previously refused to do."

It was therefore reversible error to impose the $50 fine merely to penalize in that manner the past disobedience of the order. The record clearly shows that, even though the order of June 1, 1943, had been confirmed on appeal and hence was final in every respect, the court did not intend to coerce Young into compliance therewith. This is made plain not only by the character of the judgment (R. 87), but also by concurrent statements from the bench (R. 86):

> "The Court: . . . The order will stand that the defendant be adjudged guilty of contempt.
>
> Do you have anything to say in connection with the disposition of this matter, Mr. Cuthbertson?
>
> Mr. Cuthbertson [Commission counsel]: So far as the punishment which the Court might see fit to impose, that is up to the Court. We are still anxious to get a look at these books and records, so I suggest to the Court, if he be so disposed, whatever punishment the Court might see fit to impose would be in connection with or so long as he refuses to produce his books and records for our inspection.
>
> The Court: I don't think that I am going to be disposed to do anything like that."

We have shown that the court below, upon adjudging Young in contempt, had no discretion to deny a remedial order. Furthermore, even assuming *arguendo* that there was room for discretion in this case, it is clear that the reason given by the court for refusing a coercive order afforded no valid basis for such refusal. The colloquy between the court and counsel for the Commission (R. 86-7) indicates that the court's refusal to impose a remedial

penalty was based upon its opinion that in the criminal trial of Penfield, Young and others:[4]

> "the evidence was clear and definite and positive from all of the Government's witnesses, that during one period of time this defendant [Young] had nothing whatsoever to do with the Penfield Company. Whether that period of time is covered by what the Securities and Exchange Commission seeks or not, I don't know."

The continuity or extent of Young's association with Penfield furnished no justification for refusing to render a coercive decree calculated to obtain compliance with the district court's order of June 1, 1943, affirmed by this Court.[5] Young, as an officer of Penfield, was subpœnaed to produce Penfield's books and record, not his own. The district court's order directed that they be produced for the Commission's inspection. Young's guilt or innocence with respect to any new violation uncovered in an examination of the books has no bearing on the only issues which were before the court, viz., whether Young was able to comply with the mandate, and whether his failure to comply was wilful. *Oriel* v. *Russell*, 278 U.S. 358 (1929). The court below by finding Young in contempt indicated that in its judgment he was able, but wilfully refusing, however, to produce the books (R. 85, 86). Hence, as we have shown, the court erred in failing to grant a remedial decree.

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[4] This trial was upon an indictment returned in the District Court for the Southern District of California on September 29, 1944 (No. 17230), charging violations of the Securities Act (Section 17(a) (1), 15 U.S.C. 77q(a) (1)), the mail fraud statute, and the conspiracy statute (see R. 28, 32-33, 47).

It is interesting to note that the books and records here involved were not even produced at the criminal trial to which the court adverted.

[5] Moreover, collateral attack on the subpœna enforcement order is not permissible. *Clarke* v. *Federal Trade Commission*, 128 F. 2d 542 (C.C.A. 9, 1942); *E. Ingraham Co.* v. *Germanow*, 4 F. 2d 1002, 1003 (C.C.A. 2, 1925). We have some difficulty, in any case, in understanding how the court could know in advance of the examination of the records in question, what, if anything, they would show.

The court below may have been actuated by some feeling that disposition of the criminal case prior to July 2, 1945, when the court finally heard and ruled on the order to show cause, rendered moot the application for a remedial decree (R. 86; cf. R. 48, 72). Actually, it is evident that legally the application is not moot. The date of the subpœna (April 9, 1943) shows clearly that the statute of limitations has not barred further prosecution, and the books may furnish leads to later violations. Moreover, as shown below, other proceedings are still open.

In any event, it should not lie in the mouths of appellees to object to enforcement of the district court's order on the ground of possible fruitlessness of the inquiry when their own obstructive tactics have thus far prevented the examination of the books. Certainly, appellee's contumacy makes it all the more important that the Commission be given every opportunity to scrutinize the books and records for such evidence as they may afford in aid of its investigation. Surely the delay caused by appellee's wilful disobedience should not result in any restrictive forecasts of the probable results of the examination of the books. Otherwise appellees would be profiting from their own wrong.

The Erroneous Order Not Only Results in Defeating the Commission's Investigatory Powers Under the Act, But It Also Tends to Negate the Authority and Finality of Judicial Orders Confirmed on Appeal.

The Commission's investigation has sought to ascertain the facts disclosed by the books in question. These facts alone or in conjunction with other evidence might justify injunctive proceedings by the Commission (R. 67-68), administrative proceedings before the Commission, or further criminal proceedings by the United States Attorney against Penfield, Young or any other persons or companies who may be shown to have violated the Act (R. 48, 75). Examination of the records specified in the Commission's subpœna of April 9, 1943, and the district court's order of

June 1, 1943, may disclose violations within the period of limitations, either from the books and records alone (e.g., cancelled checks, correspondence, books of accounts, lists, etc. (see R. 12)), or from the books together with other information to which the books should furnish leads. Indeed, it is pertinent to note here that the Commission's orders for investigation herein specifically recite as being under investigation a number of persons other than those named as co-defendants in the criminal proceeding brought against Penfield and Young (R. 7-8). As this Court said in *Consolidated Mines of California* v. *S.E.C.*, 97 F. 2d 704, 708 (C.C.A. 9, 1938):

> "Investigations of the sort here under consideration are analogous to those of a grand jury. In re Securities and Exchange Commission [84 F. 2d 316 (C.C.A. 2, 1936)]; Woolley v. United States, [97 F. 2d 258 (C.C.A. 9, 1938)]. The scope of the inquiries of a grand jury, it has been said, is 'not to be limited narrowly by questions of propriety or forecasts of the probable result of the investigation, or by doubts whether any particular individual will be found properly subject to an accusation of crime. As has been said before, the identity of the offender, and the precise nature of the offense, if there be one, normally are developed at the conclusion of the grand jury's labors, not at the beginning.' Blair v. United States, 250 U.S. 273, 39 S. Ct. 468, 471, 63 L. Ed. 979."

The Commission, as the agency designated by the Congress to enforce the Act, was entitled to the support of the court in its effort to ascertain the facts. The investigative powers given to the Commission under the Act (Sections 19 to 22, 15 U.S.C. Sections 77s-v), particularly the provision giving the Commission the right to compel testimony over claim of privilege (Section 22(c)), demonstrate the legislative intent that everything possible should be done to aid the Commission to uncover the facts, and that its investigations should not be permitted to be delayed or forestalled by the contumacy of persons who have been subpœnaed to produce evidence. In the instant case appellees

have succeeded in avoiding production of the subpœnaed records even after final adjudication by the appellate courts of the Commission's right to examine the books and records. This they have accomplished by arrant disobedience of the district court's order to produce the records. The failure of the court below to enter a coercive decree would seem to countenance continued disobedience of that order.

It is submitted that the order under review tends not only to strike at the roots of the Commission's enforcement functions, but also in our view has a clear tendency to set at naught the authority of the judiciary. The power to punish for contempt for disobedience of a judicial order is inherent in the courts, and its exercise in proper cases is essential. Otherwise the judicial power would be rendered impotent. *Myers* v. *U. S.*, 264 U.S. 95, 103 (1924); *Bessette* v. *W. B. Conkey Company*, 194 U.S. 324 (1904). The courts do not look with favor upon such lessening of the authority and finality of their mandates as would seem to flow from the decision of the court below in refusing to secure compliance with the district court's order through the readily available sanction of a coercive and remedial decree. As stated in *Oriel* v. *Russell*, 278 U.S. 358, 366 (1929): "'Imprisonment to compel obedience to a lawful judicial order [must be ordered] unless it should be thought expedient to destroy all respect for the courts by stripping them of power to enforce their lawful decrees.'" The Supreme Court also said in *Gompers* v. *Bucks Stove & Range Co.*, 221 U.S. 418, 450:

> ". . . the power of courts to punish for contempts is a necessary and integral part of the independence of the judiciary, and is absolutely essential to the performance of the duties imposed on them by law. Without it they are mere boards of arbitration whose judgments and decrees would be only advisory.
>
> "If a party can make himself a judge of the validity of orders which have been issued, and by his own act of disobedience set them aside, then are the courts impotent, and what the Constitution now fittingly calls the 'judicial power of the United States' would be a mere mockery."

Moreover, as stated in *Cobbledick* v. *U.S.*, 309 U.S. 323, 325 (1940), "To be effective, judicial administration must not be leaden-footed." [6]

Affirmance by the courts of the clear right of administrative agencies to subpœna enforcement orders [7] would have no practical consequence, if respondents can delay compliance pending meritless appeals from an enforcement order, and thereafter flout with impunity a court order affirmed on appeal. Imposition of a nominal fine for contempt of an order affirmed on appeal is an even more serious threat to effective enforcement of the securities laws than failure to enter a required enforcement order in the first place. We submit that effective enforcement requires an affirmation of the clear duty of the district court to compel respect for its own enforcement order and that this can be accomplished

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[6] The district court's mistaken view that it had a wide discretion with respect to enforcement of the Commission's investigatory powers is also indicated by its several rulings postponing the contempt proceedings (R. 80-81). These postponements were granted merely because of the pendency of a criminal proceeding involving *some* of the persons under investigation by the Commission (R. 76), and despite the fact that the Commission's investigation could lead to other criminal prosecutions against the same or other persons, civil injunctive proceedings, or even administrative proceedings against persons subject thereto, such as broker-dealers registered under the Securities Exchange Act of 1934 (15 U.S.C. 78). In so doing, the court incorrectly took the position that it had discretion to postpone hearing the application for a contempt order at that time merely because the production of corporate records which the contempt proceedings sought to coerce would be usable in the pending criminal case. The fact that the corporate records might be so used against Young afforded him no basis for refusing to produce the Penfield records in compliance with the district court's order. *Sinclair* v. *U. S.*, 279 U.S. 263 (1928); *In re Verser-Clay Co.*, 98 F. 2d 859 (C.C.A. 10, 1938), cert. denied 306 U.S. 639; *In re Paramount Publix Corporation*, 82 F. 2d 230 (C.C.A. 2, 1936).

[7] *Endicott-Johnson Corporation* v. *Perkins*, 317 U.S. 501 (1943); *Penfield Co. of California* v. *S.E.C.*, *supra*; *Martin Typewriter Co.* v. *Walling*, 135 F. 2d 918 (C.C.A. 1, 1943).

only by a coercive contempt order—usually imprisonment, as we have shown, unless and until compliance is obtained. Indeed, if contumaceous disobedience of a court order enforcing a subpœna issued by the Commission is susceptible of being brushed aside, as has been done in the instant case, the Commission's investigatory powers under the Act would surely be "frittered away in constant delays and failures of enforcement of lawful orders." *Oriel* v. *Russell*, 278 U.S. 358, 363 (1929).

CONCLUSION

For the foregoing reasons the order of the court below fining Young $50 should be reversed, and the court directed to enter an appropriate remedial decree calculated to secure compliance with the order to produce the records in question.

Respectfully submitted,

ROGER S. FOSTER,
Solicitor,

ROBERT S. RUBIN,
Assistant Solicitor,

W. VICTOR RODIN,
Attorney,

Securities and Exchange Commission,
18th and Locust Streets,
Philadelphia 3, Pennsylvania.

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